

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
SAM & RAJ APPLIANCE DISCOUNT CENTER, INC.	:	
For Revision of a Determination or for Refund	:	
of Sales and Use Taxes under Articles 28 and 29	:	
of the Tax Law for the Period December 1, 1981	:	
through February 28, 1986.	:	

In the Matter of the Petition	:	
of	:	
SUBHASH K. KAPADIA, AS OFFICER OF SAM & RAJ APPLIANCE DISCOUNT CENTER, INC.	:	DETERMINATION
For Revision of a Determination or for Refund	:	DTA NO. 808994,
of Sales and Use Taxes under Articles 28 and	:	812102 and 812103
29 of the Tax Law for the Period December 1,	:	
1981 through February 28, 1986.	:	

In the Matter of the Petition	:	
of	:	
NITIN VORA, AS OFFICER OF SAM & RAJ APPLIANCE DISCOUNT CENTER, INC.	:	
for Revision of a Determination or for Refund	:	
of Sales and Use Taxes under Articles 28 and	:	
29 of the Tax Law for the Period December 1,	:	
1981 through February 28, 1986.	:	

Petitioners, Sam & Raj Appliance Discount Center, Inc., c/o Arnold D. Roseman, Esq.,
670 White Plains Road, Scarsdale, New York 10583, Subhash K. Kapadia, officer of Sam &
Raj Appliance Discount Center, Inc., 16 Bristol Hills Drive, North Hills, New York 11030 and
Nitin Vora, officer of Sam & Raj Appliance Discount Center, Inc., 1063 Maple Lane, New
Hyde Park, New York 11040, filed petitions for revision of determinations or for refund of sales

and use taxes under Articles 28 and 29 of the Tax Law for the period December 1, 1981 through February 28, 1986.

A hearing was held before Thomas C. Sacca, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York on June 14, 1995 at 9:15 A.M. Petitioners filed their initial brief on August 15, 1995. The Division of Taxation filed its brief on September 20, 1995 and petitioners filed their reply brief on October 17, 1995, which date began the six-month period for issuance of this determination. Petitioners appeared by Arnold D. Roseman, Esq. The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Kathleen Church, Esq., of counsel).

ISSUES

I. Whether the Division of Taxation properly determined additional sales and use taxes due from Sam & Raj Appliance Discount Center, Inc. for the period at issue.

II. Whether Sam & Raj Appliance Discount Center, Inc. has shown that its failure to pay sales tax due was due to reasonable cause and not due to willful neglect.

III. Whether the notices of determination issued by the Division of Taxation to the officers should be cancelled because they were not received by such officers.

FINDINGS OF FACT

1. Petitioner Sam and Raj Appliance Discount Center, Inc., operated a business which sold appliances and electronic equipment at retail. Subhash Kapadia and Nitin Vora were the president and vice-president of the corporation, respectively.

2. On August 10, 1984, the initial auditor assigned to this case mailed an appointment letter to the corporation requesting that all books and records pertaining to the corporation's sales tax liability for the period under audit be available on the appointment date. The books and records were to include journals, ledgers, sales invoices, purchase invoices, cash register tapes, exemption certificates, etc., and all sales tax records. The appointment letter stated the audit period to be September 1, 1981 through May 31, 1984.

On August 22, 1984, Mr. Seymour Finder, the taxpayers' representative and the corporation's accountant, informed the auditor that a prior audit was still ongoing and he would prefer to wait for the completion of that audit before commencing this new audit. A new auditor who would eventually complete the audit was assigned to this matter on April 22, 1986. Little had been accomplished on the audit to this point in time except the signing of two consents extending the period of limitations for assessment of sales and use taxes under Articles 28 and 29 of the Tax Law. Collectively, the consents extended the period of limitation for the period December 1, 1981 through February 28, 1983 to June 20, 1986. Upon contacting the representative, the new auditor received the same message, that the representative still insisted that the audit should be placed on hold pending the completion of the earlier audit.

Finally, on February 14, 1989, the auditor was provided with and examined the books and records of the corporation and requested again that certain records be provided. The records available for review included the sales and use tax returns and the related worksheets, Federal income tax returns, State income tax returns and related worksheets, depreciation schedules, general ledger, cash receipts journal, purchase journal and cash disbursements journal. All were available for the entire audit period. Records originally requested for the entire audit period but not made available included the sales journal, sales invoices, purchase invoices, cancelled checks, bank deposit slips, monthly bank statements, resale certificates, exempt organization certificates and shipping records. Mr. Finder again requested that the audit be delayed until May when the tax season would be over.

The next meeting of the auditor and the corporation's accountant was May 24, 1989. The period of the audit was extended from December 1, 1981 through November 30, 1988. The auditor completed a schedule of the sales tax returns filed by the corporation and transcribed the sales from the business's general ledger. In addition, the auditor and Mr. Finder discussed the sales and purchase records that had not as yet been provided or examined. The representative told the auditor that the business had maintained all its purchase invoices for the audit period. According to the representative, after informing the auditor that the business had between

15,000 and 20,000 sales invoices for the audit period, the auditor stated that that was too many invoices to examine and decided to pick a test period instead.

3. On the auditor's workpaper which detailed the business's quarterly sales and use tax returns filed, the auditor had placed an "X" next to the quarter June 1, 1986 through August 31, 1986 and a check next to the quarter March 1, 1988 through May 31, 1988. On the bottom of the page the auditor had placed another "X" followed by the words "sales (test)" and another check followed by the words "purchases (test)". According to the testimony of the representative, this signified that the auditor had agreed to do a test period audit using these two quarters. However, the auditor testified that the two quarters would be used as the test periods if the corporation's books and records were adequate and complete for the entire audit period. He needed to review all the purchase and sale invoices for the entire audit period before agreeing to do a test period audit. At no time during the audit was a test period audit method election form executed by petitioners and the Division of Taxation ("Division").

4. On September 1, 1989, the auditor telephoned the representative and was told that petitioners were attempting to gather the requested invoices. The representative telephoned the auditor on October 19, 1989 and advised him that petitioners were still gathering the records. The auditor received the same message from the representative in a telephone conversation of November 22, 1989. The auditor met with petitioners' representative on February 22, 1990 and was advised that the officers were still gathering the invoices.

On March 9, 1990, the auditor sent a second appointment letter to petitioner's representative which stated, in part, as follows:

"As per our meeting on February 22, 1990, it has been determined that an actual audit will be performed on the above mentioned taxpayer. Therefore, we request the following records in order to continue the ongoing audit:

1. All sales invoices for the entire audit period;
 2. All purchases invoices for the entire audit period;
- These records should be delivered to our office . . . by March 30, 1990."

On March 29, 1990 Mr. Finder telephoned the auditor to inform him that the invoices for the entire audit period would not be available as requested but the invoices for the test period

would be. The auditor advised Mr. Finder to bring in the invoices that were available. The auditor, Mr. Finder and Mr. Vora spent April 2, 1990 in the auditor's office photocopying the records of the corporation. Mr. Finder testified that there were 3,000 to 4,000 documents including sales invoices, exemption certificates, resale invoices, shipping documents, United Parcel Service ("UPS") books and purchase invoices for the other test period. However, the auditor testified that petitioner brought in only 754 sales invoices and the corresponding UPS documents.

The auditor determined that the records provided were unreliable because the shipping records (UPS books) appeared to have been altered. This determination was made by the auditor as well as his supervisor and the sales tax unit head. On June 6, 1990, the auditor referred the case to the Office of Tax Enforcement for criminal fraud review by completing an Audit Referral for Fraud form. The auditor indicated on the form that the tax liability was understated through unreported receipts and the UPS books. At this point in time, the auditor stopped all contact with the taxpayers' representative because such was the policy of the Office of Tax Enforcement. On July 16, 1990, a fraud investigator informed Mr. Finder that the corporation had been referred to the Office of Tax Enforcement. It is noted that at this point in time, no criminal prosecution has been initiated against the corporation or its two officers. In March 1993, Mr. Roseman, petitioners' representative, was provided with an explanation of the notices of determination that had been issued to petitioners.

5. Between April 22, 1986 and January 8, 1990, the corporation, by Mr. Vora, as secretary and vice-president and Mr. Kapadia, as president, executed seven consents extending the period of limitation for assessment of sales and use taxes due under Articles 28 and 29 of the Tax Law for the period December 1, 1981 through May 31, 1987 to September 20, 1990.

6. As the corporation failed to provide the auditor with the sales invoices and corresponding shipping documents and exemption certificates for the entire audit period, the auditor disallowed all claimed nontaxable sales for the period December 1, 1981 through February 28, 1986. This resulted in assessing additional taxable sales of \$11,407,488.00 and

additional sales tax due of \$941,117.77. A 25% underreporting of tax penalty was also assessed.

7. On September 19, 1990, the Division of Taxation issued to petitioner, Sam & Raj Appliance Discount Center, Inc., two notices of determination and demands for payment of sales and use taxes due covering the period December 1, 1981 through February 28, 1986 assessing a total liability of \$941,117.77, plus penalty and interest. On the same date, the Division issued to petitioner an additional Notice of Determination and Demand for Payment of Sales and Use Taxes Due for the same period assessing a penalty liability in the amount of \$21,279.06, pursuant to Tax Law § 1145(a)(1)(vi). Identical notices were issued to Nitin Vora and Subhash K. Kapadia, as responsible officers of Sam & Raj Appliance Discount Center, Inc.

8. The notices of determination issued to Nitin Vora were mailed to 56-01 Blvd. East, West New York, NJ 07093. The notices of determination issued to Subhash Kapadia were mailed to 216 Nassau Blvd., Garden City Park, NY 11040. The addresses for the two officers were obtained from Mr. Finder. On September 26, 1990, the envelopes containing the officers' notices were returned to the Department of Taxation and Finance with the indications that the officers had moved and their forwarding addresses had expired.

SUMMARY OF THE PARTIES' POSITIONS

9. Petitioners contend that the auditor violated the corporation's statutory rights and constitutional right to due process which should lead to the cancellation of the notices of determination issued to the petitioners. The various ways by which their rights were violated are as follows:

(1) failing to give notice to petitioners that the test period was being rejected and the records were not being used in the audit.

(2) accepting the test period records which waived the auditor's request to see all the records.

(3) failing to notify petitioners that the test period was being rejected denied them the option to exercise their right to demand a detailed audit.

(4) failing to notify petitioners that the case was being referred for a criminal fraud investigation only two months after the test period records were delivered to and accepted by the auditor.

(5) failing to notify petitioners that a proposed adjustment and assessment had to be made under Tax Law § 1138(a)(1) which denied petitioners an opportunity to exercise their rights.

(6) denying petitioners the opportunity to contest the proposed assessments which were based not on an audit but on a mathematical computation of assessing a tax on all nontaxable sales during the audit period. In effect, no real audit was conducted by the auditor.

(7) failing to notify petitioners' representative of an explanation of the assessments.

The Division contends that the corporation failed to produce, upon request, any documentation establishing its claimed nontaxable sales; that it failed to demonstrate any error in the calculation of the tax due; and that the notices were properly sent to the officers of the corporation because the addresses were obtained from the officers' representative.

CONCLUSIONS OF LAW

A. Tax Law § 1138(a)(1) provides, in part, that if a return required to be filed is incorrect or insufficient, the amount of tax due shall be determined on the basis of such information as may be available. This section further provides that, if necessary, the tax may be estimated on the basis of external indices. However, the Division may not utilize external indices unless it first determines that the taxpayer's books and records are inadequate for purposes of verifying sales and purchases subject to sales and use taxes (Matter of Chartair, Inc. v. State Tax Commn., 65 AD2d 44, 411 NYS2d 41, 43). If the taxpayer's records are inadequate, the Division must then select a method of audit reasonably calculated to reflect taxes due (Matter of Grecian Square v. State Tax Commn., 119 AD2d 948, 501 NYS2d 219, 221), and the burden is on the taxpayer to establish by clear and convincing evidence that the method used to arrive at the tax assessment and the assessment are erroneous (Matter of Sol Wahba, Inc. v. State Tax

Commn., 127 AD2d 943, 512 NYS2d 542, 543). Furthermore, the Tax Appeals Tribunal has noted that:

"[w]here the taxpayer establishes that the audit methodology is based on an assumption that is fundamentally flawed, the taxpayer has sustained his burden of proof and is not required to show the exact amount of taxes due [citations omitted]" (Matter of Bernstein-On-Essex, Tax Appeals Tribunal, December 3, 1992).

B. To determine the adequacy of a taxpayer's records, the Division must first request and thereafter thoroughly examine the taxpayer's books and records for the entire period of the proposed assessment (Matter of Adamides v. Chu, 134 AD2d 776, 521 NYS2d 826, lv denied 71 NY2d 806, 530 NYS2d 109; Matter of King Crab Restaurant v. State Tax Commn., 134 AD2d 51, 522 NYS2d 978). The purpose of this examination is to determine whether the taxpayer's books and records are so insufficient as to make it virtually impossible for the Division to verify taxable sales receipts and conduct a complete audit (Matter of Chartair, Inc. v. State Tax Commn., supra; Matter of Ronnie's Suburban Inn, Tax Appeals Tribunal, May 11, 1989). Where the Division follows such steps, it then may resort to external indices to estimate tax.

C. In the present matter, the auditors made a proper request for petitioner's books and records. The initial auditor made a written request in August 1984 for all of the corporation's records, including the sales invoices, while the second auditor made a specific written request for the sales and purchases invoices in March 1990. Petitioners supplied the auditor with all the books and records requested, except the invoices, exemption certificates and other source documentation, in February 1989. The second request letter was written after the auditor waited for over a year and had not received the invoices. Petitioners produced the sales invoices and shipping records only for the three months of June, July and August 1986 in April 1990. This was approximately six years after the initial request for the sales invoices was made. After reviewing these documents the auditor not only concluded that they should be reviewed for possible criminal fraud, but also concluded that the books and records were inadequate. All the other records maintained by the corporation which were requested and provided were reviewed by the auditor.

This matter was referred to the Office of Tax Enforcement in June 1990 and Mr. Finder was notified of the transfer in July 1990. No further contact was made by the auditor with petitioners' representatives after the referral as it was the policy of the Office of Tax Enforcement that he not have any contact once the case was referred.

A test period audit was not performed in this matter nor was one agreed to (a test period audit method election form was not signed), but rather the auditor attempted a detailed review of all claimed nontaxable sales. A test period audit was not to be performed until the auditor was satisfied that the books and records of the corporation were adequate and complete. The claimed nontaxable sales were deemed taxable as no nontaxable documentation was provided. Petitioner was obligated under Tax Law § 1135(a)(1) to maintain source documents, such as the sales invoices and exemption certificates, for all its transactions. It failed to do so. Under these circumstances, it was proper for the Division to rely on the presumption of taxability contained in Tax Law § 1132(c) with respect to the unsubstantiated claimed exempt sales (Matter of Academy Beer Distributors, Tax Appeals Tribunal, January 21, 1993, confirmed 202 AD2d 815, 609 NYS2d 108, lv denied 83 NY2d 759, 616 NYS2d 14).

D. In this case, there can be no legitimate challenge to the adequacy of the Division's request for and review of the corporation's books and records for the audit period. Rather, the Division made such request and reviewed the materials presented by the corporation. In fact, the Division's calculation of tax due is based on the corporation's gross sales minus the taxable sales per the books and records for the period involved. The Division assessed as taxable unsubstantiated nontaxable sales based on the corporation's inability to present documentation as requested substantiating that such receipts were not taxable as claimed.

E. Petitioners continue to claim nontaxability with regard to the sales at issue, based on alleged exemptions. In fact, petitioners' claim has become, most specifically, that eliminating the exempt sales from taxable sales will properly reduce the tax due to zero. The only real issue remaining is whether and to what extent the corporation has established proper nontaxability of the transactions at issue.

F. Tax Law § 1132(c) sets forth an initial presumption of taxability with regard to receipts such as those at issue herein, and places the burden of establishing nontaxability upon the person making such claim, i.e., the corporation (Matter of Sunny Vending Co. v. State Tax Commn., 101 AD2d 666, 475 NYS2d 896). To demonstrate that certain amounts were not subject to tax, as claimed, the corporation must be able to offer substantiation, in the type of case at hand, specifying the amounts of the particular sales and confirming that the sales were not subject to sales tax. Put another way, the corporation would be expected to present sales invoices or other records of individual sales together with related payment records.

G. At the hearing, the corporation submitted no direct documentary proof in an attempt to establish that the sales were exempt from the imposition of sales tax. The only evidence the corporation produced was the testimony of Mr. Finder to the effect that approximately 80% of the business's sales were exempt from the imposition of sales tax.

The testimony of Mr. Finder was, in general, unrelated to any specific transaction and unsupported by direct documentary evidence. There was not one example of a transaction being exempt. The sales invoices were not placed into the record of this matter nor were they provided to the auditor. No explanation for their unavailability was provided. Therefore, no adjustments to the audit findings are warranted.

H. Under Tax Law §§ 1134(a), 1135(a)(1) and 1136(a), as a person required to register, maintain records and collect sales tax, Sam & Raj Appliance Discount Center, Inc. was required to collect sales tax, maintain records of each transaction and file sales tax returns and pay the sales tax due. Its failure to collect, maintain records and pay the sales tax due justifies the imposition of penalty.

Petitioners offered no evidence at hearing to establish reasonable cause for the failure to collect and pay the sales tax due. Furthermore, the corporation's reliance on professional advice is insufficient to justify abating penalties because such reliance was not reasonable given the clarity of the legal requirements that were ignored (cf., Matter of Aire Bon Associates, Tax Appeals Tribunal, April 18, 1991). Therefore, the penalties are sustained.

I. Petitioners Subhash Kapadia and Nitin Vora offered no proof on the issue of whether they were liable for the sales and use taxes due on behalf of the corporation as persons responsible for the collection and payment of sales tax pursuant to Tax Law §§ 1131 and 1133. Therefore, they remain liable for such taxes.

J. Tax Law § 1138(a)(1) provides, in pertinent part, that:

"Notice of such determination shall be given to the person liable for the collection or payment of the tax. Such determination shall finally and irrevocably fix the tax unless the person against whom it is assessed, within ninety days after giving of notice of such determination, shall apply to the division of tax appeals for a hearing"

K. Tax Law § 1147(a)(1) provides that:

"[a]ny notice authorized or required under the provisions of this article may be given by mailing the same to the person for whom it is intended in a postpaid envelope addressed to such person at the address given in the last return filed by him pursuant to the provisions of this article or in any application made by him or, if no return has been filed or application made, then to such address as may be obtainable. A notice of determination shall be mailed promptly by registered or certified mail. The mailing of such notice shall be presumptive evidence of the receipt of the same by the person to whom addressed. Any period of time which is determined according to the provisions of this article by the giving of notice shall commence to run from the date of mailing of such notice."

L. A petitioner has the option of requesting a conciliation conference with the Bureau of Conciliation and Mediation Services ("BCMS") upon receipt of the Notice of Determination, rather than filing a petition (20 NYCRR 4000.3[a]). Such a request must also be filed within the 90-day period for filing a petition and effectively suspends the running of the limitations period for the filing of a petition (20 NYCRR 4000.3[c]).

M. Where the petition is denied as untimely, the Division is required to establish both the fact and date of mailing of the Notice of Determination (see, Matter of Montesanto, Tax Appeals Tribunal, March 31, 1994; Matter of Novar TV & Air Conditioner Sales & Serv., Tax Appeals Tribunal, May 23, 1991). The proof required consists of evidence of a standard procedure for the issuance of such notices offered by one with personal knowledge of such procedures and evidence that establishes that the procedure was followed in the particular case under consideration (see, Matter of Montesanto, Tax Appeals Tribunal, March 31, 1994; Matter of Accardo, Tax Appeals Tribunal, August 12, 1993; Matter of Katz, Tax Appeals Tribunal,

November 14, 1991; Matter of Novar TV & Air Conditioner Sales & Serv., *supra*; *see also*, Matter of MacLean v. Procaccino, 53 AD2d 965, 386 NYS2d 111; Cataldo v. Commissioner, 60 TC 522, *affd* 499 F2d 550, 74-2 US Tax Cas ¶ 9533).

N. Here, there was no proof offered of the fact and date of mailing of the notices. More importantly, it is without question that the two individuals did not receive the notices of determination, as the envelopes which contained the notices issued to the officers indicate nonreceipt by the addressees. Therefore, there can be no presumption of receipt under these circumstances.

O. However, it is noted that no relief is warranted in this matter. In those instances where the notice is not received, the only remedy is to afford the taxpayer additional time to file a petition to protest the notice (*see*, Matter of Ruggerite, Inc. v. State Tax Commn., 97 AD2d 634, 468 NYS2d 945, *affd* 64 NY2d 688, 485 NYS2d 517). Since there is no issue with respect to the timeliness of the petitions, no further relief on this point is warranted.

P. The petitions of Sam & Raj Appliance Discount Center, Inc., Subhash Kapadia and Nitin Vora are denied and the notices of determination, dated September 19, 1990, are sustained.

DATED: Troy, New York
April 4, 1996

/s/ Thomas C. Sacca
ADMINISTRATIVE LAW JUDGE